



September 22, 2003

## The President's Reconstruction Request for Iraq and Afghanistan Should Be Supported

### *Summary*

- On September 17, the White House sent to Congress the following request for \$87 billion in supplemental funding for military operations and reconstruction efforts in Iraq and Afghanistan.

#### **\$65.6 billion for Department of Defense and Classified Activities:**

- Approx. \$51 billion, *Operation Iraqi Freedom*;
- Approx. \$11 billion, *Operation Enduring Freedom*; and
- Approx. \$4 billion, *Operation Noble Eagle* and support for allies in the war on terror.
- These monies support military operations, personnel and health care costs, military construction, equipment procurement, and maintenance.

#### **\$21.4 billion for Coalition Provisional Authority and Department of State:**

- Approx. \$20 billion for Iraq—
  - \$5 billion (border enhancement, national police force, Iraqi army, judiciary);
  - \$6 billion (basic electricity services);
  - \$4 billion (water and sanitation services);
  - \$4 billion (transportation, telecommunication, housing, health, education); and
  - \$2 billion (oil infrastructure rehabilitation).
- Approx. \$800 million for Afghanistan—
  - Afghan National Army creation and Kabul-Herat road construction.
- U.S. assistance funds Free Iraqis, an alliance of nearly 56,000 soldiers and police fighting and risking their lives to bring stability to Iraq, which serves as the largest coalition partner working alongside U.S. forces in *Operation Iraqi Freedom*.
- By providing Iraq with \$20 billion in reconstruction aid, the U.S. is providing resources to meet urgent basic humanitarian, infrastructure, and security needs; provide employment opportunities; better social conditions; and make progress in handing over daily government operations to the Iraqi government. This will create the conditions for the eventual withdrawal of U.S. troops.
- Ambassador L. Paul Bremer, the Coalition Provisional Authority Administrator in Iraq, has stated that Iraq will need an estimated \$50 billion-\$75 billion in capital investment; the U.S. contribution toward this will be \$20 billion. International support is expected in October at the international donors conference in Spain. Moreover, as the economy begins to function, Iraqis themselves will bear responsibility for reconstructing their economy.

## **Why Reconstruction Monies Should be Granted, Not Loaned**

It has been suggested that the President's request of \$20 billion in Iraqi reconstruction monies be awarded as a loan, and not a grant, with future Iraqi oil revenues reimbursing present domestic reconstruction efforts. The President has proposed that the supplemental funding be provided in the form of an unconditioned grant, and that the oil revenues be used to complement the U.S. contribution, not as repayment. Among the primary reasons are:

### **There Are Likely To Be No Savings Associated With A Loan To Iraq**

When the Congress authorizes the provision of loans, a certain amount must be set aside as a subsidy for the loan, in essence to insure against default. This amount is calculated based upon the creditworthiness of the loan recipient. According to the Office of Management and Budget and the Congressional Budget Office, given Iraq's weak commercial credit rating, a \$20 billion loan would require a subsidy appropriation of close to \$20 billion, or nearly 100 percent. In other words, there are little if any savings associated with a loan.

### **U.S. Needs To Have Flexibility In How Funds Are Distributed**

By providing reconstruction monies as a loan, it is quite likely that conditions and restrictions would be placed on these monies, thus reducing the ability of Ambassador Bremer, the Coalition Provisional Authority Administrator, Lt. General Abizaid, the commanding general in charge of U.S. forces in Iraq, and other officials to make funds available for urgently needed security and reconstruction projects. Stabilizing Iraq as quickly as possible will reduce threats to our soldiers.

### **Iraqis Need Assistance In An Uncomplicated Manner**

Multi-billion-dollar loans will add stress to the already deeply indebted Iraqi economy. Given the likelihood that it will take at least a few years before the Iraqi oil infrastructure is repaired, updated, and generating positive revenues, the new Iraqi government will be making considerable interest-only payments derived from a limited agricultural and service-based economy.

Moreover, such a massive loan burden would saddle future generations of Iraqis with huge interest and principal payments, and would likely stifle any significant economic development as well as discourage private investment. If a stable and prosperous free Iraq does not emerge, additional U.S. aid and assistance will be needed for years to come.

### **Marshall Plan Not Based on Overriding Premise: "We Rebuild You; You Owe Us"**

Getting the reconstruction of Iraq right is just as important as getting post-World War II reconstruction of Europe right. Arguably, the vast economic potential of a rebuilt Europe was foreseen by Secretary of State George Marshall and his colleagues. It was the political, social, and democratic potential of a rebuilt and free Europe embracing liberal government and serving as an ally in a region consumed with tyranny that convinced Marshall that America could not place unrealistic economic burdens and debts on Europe.

Moreover, Marshall and others had witnessed the consequences of the post-World War I victors' decision to place undue economic costs, i.e., Allied war reparations, on Weimar Germany, a nation thoroughly defeated, humiliated, and devastated following the Great War. By placing such a burden on the German economy and people, the conditions were ripe for the rise of popular discontent and fanatical extremist movements. The virtue of the Marshall Plan was proven when Europe, which for a thousand years had been the engine of war in the world, has, in the past half century, become an engine of peace, stability, and prosperity. Thus, if the United States really wants to help the Iraqi people to achieve stability and prosperity—to the extent that there is no longer a need for U.S. troops in Iraq—it can best be accomplished by providing unencumbered funding.

### ***If U.S. Provides Monies As Loan, Other Donor Nations Likely Will Seek Same Terms***

Currently, Iraqis are burdened with an estimated \$100 billion in Hussein-era debt, with France, Germany, and Russia being the largest holders of that debt. Not only would additional loans add billions in interest payments, it would likely preclude grants from Moscow, Paris, and Berlin, and also likely preclude those countries from considering forgiving or reducing the debt owed to them. By making reconstruction monies available in the form of an unconditioned grant and not a loan, America increases its leverage in calling on other countries to contribute to the Iraq effort, as well as to write off past debts. This will be a key factor in October at the international donors conference in Spain, where coalition partners and other nations are expected to pledge additional billions in reconstruction aid.

### ***Requiring Iraq To Repay U.S. Reconstruction Assistance Lends Credibility To Those Who Wrongly Argued That The United States Attacked Iraq To Gain Access To Oil***

On April 8, 2003, President Bush and British Prime Minister Blair issued a statement regarding the future of Iraq. In it they declared, “We reaffirm our commitment to protect Iraq’s natural resources, as the patrimony of the people of Iraq, which should be used only for their benefit.” The Bush Administration recognized that U.S. interests in Iraq lie solely with the development of a free and democratic nation. Congress should not now add a condition of our involvement that suggests the United States had an interest in Iraqi oil all along. Using Iraq’s oil as collateral for loans would play into the hands of those who wrongly attributed an “oil motive” to President Bush’s decision to take action in Iraq.

## **Democrats Want to Pay for Supplemental with Repeal of Tax Relief**

The suggestion by some that Congress should fund the President’s Iraq supplemental funding request by repealing the Bush tax relief for the top 1 percent of wage earners is inherently unfair and economically unsound. The top 1 percent of wage earners in the United States already pay the vast majority of income taxes – an amount that most Americans believe is unfair. Just as importantly, they represent a significant component of economic growth in this country. Many of these wage earners are the entrepreneurs who create wealth and jobs for all Americans; increasing the tax burden of these job creators will simply limit their ability to generate economic activity, slowing the nation’s economic rebound.

### **Top One Percent of Taxpayers Pay a Disproportionate Share of Income Taxes**

As the following chart demonstrates, in 2000 the top 1 percent of wage earners in America pay an extremely disproportionate share of income taxes.

<b>Percentiles Ranked by AGI</b>	<b>AGI Threshold on Percentiles</b>	<b>Percentage of Federal Personal Income Tax Paid</b>
Top 1 Percent	\$313,469	37.42
Top 5 Percent	\$128,336	56.47
Top 10 Percent	\$92,144	67.33
Top 25 Percent	\$55,225	84.01
Top 50 Percent	\$27,682	96.09
Bottom 50 Percent	\$27,682 and Less	3.91
Note: AGI is Adjusted Gross Income Source: National Taxpayers Union; calculations from 2000 IRS figures		

This represents a far greater amount than Americans believe they should pay in *total* taxes, let alone income taxes solely. A recent paper by the American Enterprise Institute on Americans' opinion on taxation cites a January, 2003 Fox News/Opinion Dynamics poll showing that Americans do not believe any American – even the wealthiest – should pay more than 17 percent of his salary in total taxes (on average).<sup>1</sup>

### **Many in Top One Percent are Small Business Owners, Vital to Economic Growth**

Economically speaking, raising taxes on the top 1 percent of wage earners would deal a significant blow to our economic recovery. As Vice President Cheney noted on a recent appearance on *Meet the Press*, a sizeable number of Americans in the top 1 percent of wage earners are small businessmen – a vital component to America's economic health. The Vice President noted, "If you're going to go increase taxes on small businesses, you're going to slow down the extent to which we're able to reduce unemployment."<sup>2</sup>

In fact, a recent study by the Joint Economic Committee found that small businesses are responsible for approximately 36 percent of total employment and "are important not only for the

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<sup>1</sup> AEI Studies in Public Opinion, "Public Opinion on Taxes," updated June 4, 2003, <http://www.aei.org/publication16838>.

<sup>2</sup> NBC News, *Meet the Press*, September 14, 2003.

jobs they provide, but also for the investment they undertake, spurring economic growth.”<sup>3</sup> The study also notes that lower marginal income-tax rates encourage small businesses to increase investment and employment.<sup>4</sup>

The fact is, the Bush tax relief passed this spring is the very reason the economy is beginning to recover – enabling taxpayers to afford to contribute to the rebuilding of Iraq. Reversing course and repealing a major component of that economic recovery plan will spell economic disaster at home and seriously impair the ability of the United States to successfully complete our mission in Iraq.

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<sup>3</sup> Joint Economic Committee, “How the Top Individual Income Tax Rate Affects Small Businesses,” May 6, 2003.

<sup>4</sup> Joint Economic Committee.